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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1952.

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

v.

RALSTON PURINA COMPANY.

SUGGESTIONS

Of Ralston Purina Company in Opposition to the
Petition of the Securities and Exchange Com-
mission for a Writ of Certiorari.

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The Securities and Exchange Commission has asked this Court to issue its writ of certiorari to review the judgment of the United States Court of Appeals for the Eighth Circuit, dated November 21, 1952, which affirmed the judgment entered on February 20, 1952, by the United States District Court for the Eastern District of Missouri, Eastern Division.

The Commission prays for the issuance of its writ on the ground that the opinion of the Court of Appeals for the Eighth Circuit is in conflict with the opinion of the Court of Appeals for the Ninth Circuit in the case of Se-

curities and Exchange Commission v. Sunbeam Gold Mines Company, 95 Fed. 2d 699, and on the further ground that the opinion of the Eighth Circuit Court erroneously reverses a long standing administrative interpretation by the Commission.

We respectfully submit that the opinion which the Commission is asking this Court to review is not in conflict with the opinion of the Ninth Circuit and that it does not reverse any long standing administrative interpretation.

This litigation was instituted by the Securities and Exchange Commission to enjoin Ralston Purina Company from selling its \$25 par value common stock to certain of its employees, claiming that such sale would be in violation of the registration requirements of Section 5 (a) of the Securities Act of 1933. The Ralston Company consented to the issuance of a temporary restraining order, filed its answer, and the case was heard and tried in the United States District Court for the Eastern Division of Missouri. The only witness who testified orally in the District Court was Mr. Lewis B. Stuart, Vice President, Secretary, and a director of the Ralston Company, and, as later pointed out in the opinion of the Court of Appeals (R. 89-90), the evidence in the case was virtually undisputed. And on February 20, 1952, the Honorable Ruby M. Hulen, Judge of the District Court, after filing a memorandum opinion in which he made findings as to the evidence, and pursuant to such opinion, dismissed the petition. Appeal was taken by the Commission, and the United States Court of Appeals for the Eighth Circuit, speaking through Judge Sanborn, handed down a unanimous decision which affirmed Judge Hulen's opinion in the District Court. Pending the appeal from the District Court, the Ralston Company stipulated that it would not sell or offer to sell any of its stock pursuant to its original plan until the case had been finally determined.

STATEMENT.

The Ralston Purina Company was organized in 1894 and has approximately 7,000 employees. Its net sales for fiscal 1951 exceeded \$340,000,000 and it operates 36 feed mills, 6 soy bean processing plants, and 3 cereal mills, and also operates many warehouses and elevators and 79 retail stores (R. 57). The Company has continuously followed the policy of promoting its personnel from within. From the inception of the Company (at least as far back as 1911), it has had a policy of encouraging stock ownership by key employees (R. 57). Key employees were defined by Mr. Lewis B. Stuart, Vice President, Secretary, and Director, and chief financial officer, as follows:

"A key employee, of course, can be an officer or a department head or an assistant to a department head, but is not confined to an organization chart. It would include an individual who is eligible for promotion, an individual who especially influences others or who advises others, a person whom the employees look to in some special way, an individual, of course, who carries some special responsibility, the management feels is likely to be promoted to a greater responsibility" (R. 58).

The Company has approximately \$10,000,000 of preferred stock outstanding which was underwritten and sold to the public after registration with the Commission. Its \$25 par value common stock (1,229,712 shares) is unlisted, but is dealt in to a certain extent in the over-the-counter market. Particularly since 1942 the Company has offered stock ownership to employees who could meet its test of key employees, and each year has made large bonus payments (for example, in fiscal 1951, \$1,575,000) to its key employees whom the management felt had made a special contribution (R. 59). The reason for selling stock

in limited quantities, to such employees was that the Company felt that it created a greater efficiency because it drew employees closer together, and many of its employees came from the rural areas where proprietorship was a matter of pride to them and the fact that they were at least part owners contributed to their morale and the morale of the Company (R. 58). Stock was made available to these key employees at the end of the fiscal year for the reason that if the key employees whom the Company knew wished to have stock were required, in order to get stock, to bid against each other in the limited over-the-counter market, it would artificially run the price up unreasonably, whereas, when stock was made available to such key employees by the Company at or about the over-the-counter market price, such key employees could use their bonuses to obtain such stock without forcing the market up artificially (R. 59). It was the projected sale of stock to such key employees in the year 1951 which was temporarily enjoined by the Commission and which is now involved in this suit.

The Ralston stock was sold to and bought by these key employees for investment and not for resale or distribution. The District Court's memorandum opinion found it to be a fact that only 17 such employees who purchased this stock in 1947 thereafter sold it, none in 1948, 9 in 1949, and only 4 in 1950, and that such sales in most instances were by persons who had left the Ralston employ at time of sale (R. 48).

In its petition for a writ of certiorari the Commission, as it did in the Court of Appeals, sets forth a number of statements and inferences or conclusions which it wishes to draw from the record which are not supported by the record, and we believe it necessary to point out such statements, inferences or conclusions to this Court and also to

point out wherein it appears that they are erroneous and unsupported by the record.

1. The statement is made on page 5 of the petition that the evidence indicates that the Company used the term "key employees" to include any employee who might have "indicated an interest in the purchase of stock"; and on page 10 substantially the same statement is made that the offering of the Ralston stock was open to any employee who expressed an interest in purchasing it. And again the statement is made at the bottom of page 5 and the top of page 6 that the Company's branch managers indicated that any employees taking the initiative might buy the stock. These inferences or conclusions are directly contrary to the record and to the findings of the District Court and the Court of Appeals. Mr. Stuart, the Company's Vice-President in charge of finances, testified positively and without contradiction that offerings or sales of stock to employees of the Ralston Company had always been limited exclusively to key employees (R. 58). And the District Court found it to be a fact that no common stock was ever sold to any employees except those who were designated as key employees, and only key employees were advised by managers and various department heads that such stock was available for purchase by them (R. 49). In his memorandum opinion the District Court made the following specific findings (R. 54):

"The circumstances of the plan of offering stock to 'key employees' lacks the slightest suggestion of a device to evade the law invoked by plaintiff. The offering has a lawful purpose entirely independent from the objective of the law.

"Plaintiff emphasizes the failure of the resolution by terms to confine the offering to 'key employees'. This is the same type of resolution defendant has used for like offerings in previous years. The resolution is

not the offering—it is authority for the offering. What was done—the facts regarding the manner and reason for the offering, rather than the resolution, show the nature of the offering to be private. Those facts are not in dispute.”

And again on page 10 the petition for certiorari states that the offering was open to any employee who expressed an interest in purchasing the Ralston stock. As we have already pointed out, this is directly contrary to the facts as shown by the record, as found by the District Court, and as found by the Court of Appeals, that never at any time was any stock offered or sold to any employee except those who had actually been classified as “key employees”.

2. And on page 2 of the petition under the heading “Question Presented”, the statement is made that “the offering here involved was made to an indeterminate group of more than 500 employees, including those who had no access to information concerning the issuer’s affairs.” The only testimony as to the number of employees involved is that of Mr. Stuart that no record was kept of the persons to whom the stock was made available, but that his best estimate would be that it was made to between 400 and 500 employees. The District Court in his memorandum stated in this regard (R. 47) that “it (i. e., the Ralston Company) estimated the offering for the year 1951 to have been made to approximately 500 key employees, or 5% to 8% of the total employees”. The statement in the petition that the offering was made to employees who had no access to information concerning the issuer’s affairs is misleading and inaccurate because the undisputed evidence was that more than 75% of the key employees to whom the offering was made were already stockholders of the Company (R. 59). And it was likewise undisputed that the Company’s balance sheet and earnings statement was sent to all stockholders and to banks, investment brokers,

and to the Commission (R. 60). And it was also undisputed that the Ralston Company printed bi-monthly bulletins which were sent to all branches, warehouses, and stores and posted or made available to all employees; and that such bulletins showed the amount of tonnage which the Company was currently producing and selling (R. 48).

3. On page 12 of the petition the word "deceptive" is used. In connection with the use of this word the Commission is evidently undertaking to answer the finding of the District Court and the Court of Appeals that about 75% of the employees purchasing stock were already stockholders and that annual reports were sent to all stockholders, and that sales and production figures were regularly published bi-monthly on the bulletin boards of the Company's places of business; that such information as to such sales and production were made available bi-monthly to all employees. And the claim is being made that the sales and production figures were "deceptive as a measure of profit". In connection with the use of the word "deceptive", petitioners refer to the Exhibit found on page 82 of the record which shows that the Company's annual statement for fiscal 1951 shows that although sales had increased from \$253,000,000 in fiscal 1950 to \$342,000,000 in fiscal 1951, the net income after taxes fell from \$12,560,000 in fiscal 1950 to \$8,784,000 in fiscal 1951. The Exhibit itself, however, affirmatively shows that the fall in net earnings from the previous year was due entirely to two things: the excess profits tax for fiscal 1951, plus an additional \$500,000 excess profits tax due for fiscal 1950. In other words, the only thing that reduced the net earnings in fiscal 1951 was the heavy inroads that excess profits taxes were making on corporate profits, and we submit that it was an improper statement for the Commission to make in this petition that the sales and production figures were "deceptive".

4. The most flagrantly unwarranted statement made in the petition is the one on page 16 where it is said that persons to whom this stock was offered were persons "picked almost at random". This statement is directly contrary to every bit of evidence in the record. It is directly contrary to the findings of the District Court and the Court of Appeals, and it is so unwarranted and unsupported by the record that we have difficulty understanding how such a statement could have been made by the Commission in its petition.

We have felt it necessary to point out to the Court the erroneous statements, inferences and conclusions appearing in the petition for the writ. We have not undertaken to make a full statement of all the facts because they appear in the record and in the memorandum opinion of the District Court and the opinion of the Court of Appeals. We very respectfully request this Court to examine them.

We pass on briefly to the petitioner's contention that the opinion of the Court of Appeals in the instant case is in conflict with the opinion of the Ninth Circuit in the Sunbeam Gold Mines case, 95 Fed. 2d 699. We do not quarrel with either the principle of that case nor the result, but the facts before the Court there were not comparable to those presented here. The Sunbeam Company had stockholders in various states. It entered into an agreement with another company, the Golden West Consolidated Mines, to purchase or acquire through merger all the assets of the latter company. While the agreement was pending, the Sunbeam Company sent through the mails letters to 530 different persons, 115 of whom were its own stockholders, 207 were stockholders of the Golden West Company, and 208 were stockholders of both companies. Those letters solicited pledge loan agreements for the purpose of completing the purchase by Sunbeam of the assets and to raise

money to register contemplated new issue of stock with the Securities and Exchange Commission. Upon signing the pledge loan agreement, each stockholder was to receive a "shareholder's receipt," stated by the Court to be in effect a promissory note of Sunbeam and therefore a security. It was contended there by the Sunbeam Company that because the offer was made only to the 323 stockholders of the offering company and the 207 stockholders of the Golden West Company, it was a private rather than a public offering. The Court of Appeals rejected that contention and said that such a distinction was inadequate for practical reasons (l. c. 701). It went on to say "such an offering, though not open to everyone who may choose to buy, is nonetheless 'public in character,' for the means used to select the particular individual to whom the offering is made bears no sensible relation to the purposes for which the selection was made" (l. c. 701). In the Sunbeam case, the offer was made to raise money for the business and in the instant case it was made to cement employee relationships so as to bring about a closer and more direct interest by the employees in the Company's operations. The Sunbeam case was analyzed and discussed very carefully both in the opinion of the District Court and that of the Court of Appeals. Both Courts carefully distinguished between the factual situation in the two cases and not only did not criticize the decision of the Ninth Circuit, but affirmatively approved it, and held that the situation in the instant case is so different from the facts in the Sunbeam case that a different conclusion must be reached. We refer this Court to the analysis of the Sunbeam case which will be found in the District Court's opinion (R. 51-52). This distinction was emphasized in the opinion of the Court of Appeals as follows (R. 99):

"Our opinion is strictly confined to the precise facts here involved and is not to be taken as a ruling that employees' stock investment plans are generally

within the exception granted by Section 4 (1). If the offering with which we are concerned were made to all employees or employees selected by random or by lot or without any logical basis for the selection, a different question would be presented."

We refer now briefly to petitioner's contention that the decree of the Court of Appeals reverses a long standing administrative interpretation by the Commission. The petitioner here is referring to and cites an opinion of its counsel in 1934 (Footnote, R. 96-100). Apparently the opinion of the Commission's counsel was in reference to a particular case which was presented and his opinion closes by saying that it was a wiser policy not to express an opinion in the situation presented to him (R. 100). As regards this opinion of counsel, it should first be pointed out that it was an interpretation not of rules and regulations promulgated by the Commission, but of the law itself which had been passed by Congress. And in the case of *Norwegian Nitrogen Products Company v. United States*, 288 U. S. 294, 1. c. 325, Mr. Justice Brandeis, in referring to the Federal Trade Commission, said, "the Commission was without competence by any decision it might make to fix the meaning of the phrase **as used by Congress** or the courts. It had power, however, to interpret its own rules and any phrase contained in them." (Emphasis supplied.) The Commission in this case is not relying upon an interpretation of a rule or regulation of the Commission, nor is it even relying upon its own interpretation. It is placing its reliance upon an opinion written by the Commission's former counsel and giving his own opinion as to the factors which should be considered in determining whether or not a public offering exists.

It will also be noted that the counsel's opinion lays down no specific test of numbers, and the specific tests which

counsel does propose are, we submit, met by the Ralston Company in this case. The opinion stresses the number of units offered and the size of the offering because such factors indicate whether or not a public distribution of the securities involved is contemplated. The evidence is clear and undisputed that no public distribution of the Ralston Company stock sold to its key employees was either contemplated or made. Out of a total of 27,763 (R. 11, 18, 19, 29) shares sold to key employees during the years 1947 to 1950, 27,312 (R. 44-45) are still held by the original purchasers and the only resales made were by a few individuals for private reasons (R. 48). Another test given in the Burns opinion is the manner of the offering and there he states that transactions which are effected by direct negotiations by the issuer are much more likely to be non-public than those effected through the use of the machinery of public distribution. No such machinery was used here. A further test and the most important of all in this case is stated in his opinion to be the basis on which the offerees are selected and the relationship between the issuer and the offeree. This last test is particularly stressed in the opinion of the District Court and again in the Court of Appeals. Both opinions consider at length and stress the fact that there existed in this case "a sensible relation to the purpose for which the selection of offerees was made" (R. 53, 98). The trial judge gave great weight to the undisputed fact that the offering was in strict accordance with the Company's consistent policy for many years of securing competent management from within its organization by promotion and encouragement and had found that the selection of offerees was for the purpose of keeping part ownership of the business in the hands of its operating personnel and to secure such ownership from among the key employees throughout the various departments. Again, the District Court's opinion stresses that (R. 52-53):

"The circumstances of the offering under examination are plainly and frankly spread before the Court. They involve no promotion or cash-raising scheme by the defendant. They are the same circumstances that have surrounded a like activity for several years past. Defendant has followed a consistent policy of securing its managerial and executive personnel by promotion within the organization. Without competent management any business must fail. The success of defendant testifies to the soundness of its policy. It desires to continue the policy.

"The sole purpose of the 'selection' is to keep part stock ownership of the business within the operating personnel of the business and to spread ownership throughout all departments and activities of the business. No greater tie, to secure loyalty, could be forged between the corporation and its employees than part ownership in the business by the employees. It is an appeal to the employee's self-interest, but a commendable one. Defendant could confine stock offerings to those high in the executive positions, but that would not accomplish its long range purpose of bringing from the ranks those who represent good prospects for company management. Defendant chooses to call such prospects, together with those who are in executive positions, 'key employee.' Doubtless the name was suggested by the thought that such character of employees is the key to the company's success, past and present. We have examined defendant's definition of 'key employee' and see nothing hypocritical or evasive in it. We do not need expert testimony to understand the purpose of the definition and its application to a private enterprise. Both in accord with sound business policy. Under the definition it calls for an observation of employees whom the company considers 'eligible for future promotion to a position of greater responsi-

bility' in the various departments. They consider whether the prospect is 'ambitious and likely to develop and grow with the Company's business' and who has a beneficial or 'special influence' among other employees, and one who is 'sympathetic to management' and has the interests of the employer at heart. No better way has been suggested to find 'key employees,' that is employees who look like good prospects as part owners to carry on and promote the success of the company. What motive could the defendant have for such a policy other than the one announced? None has ever been suggested. The purpose of the selection bears a 'sensible relation' to the class chosen."

CONCLUSION.

We respectfully submit that the opinion of the Court of Appeals is not in conflict with the opinion of the Ninth Circuit does not "erroneously reverse a long-standing administrative interpretation," and will not in any wise prevent the Commission from carrying out the purpose and intent of the Securities Act. We therefore submit that the petition for certiorari should be denied.

Respectfully submitted,

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